



**NORTH DAKOTA
FIRST TIME FARMER FINANCE PROGRAM
SUMMARY**
July 31, 2009

**NORTH DAKOTA FARM FINANCE AGENCY
BANK OF NORTH DAKOTA
1200 MEMORIAL HWY
PO BOX 5509
BISMARCK ND 58506-5509**

**PHONE 1-800-472-2166
EXT 5786
FAX 701 328-5731**

www.banknd.nd.gov

TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
THE PROGRAM SUMMARY IN BRIEF	1
I PROGRAM POWERS AND ELIGIBLE ACTIVITES	1
1. Agricultural Land	1
2. Agricultural Improvements	1
3. Depreciable Agricultural Property	1
II PROGRAM MAXIMUMS AND MINIMUMS	2
III NATURE OF INVESTMENT RISK; LIMITED OBLIGATION BONDS	2
IV APPLICANT ELIGIBILITY	2
1. Age Limits	2
2. First Time Farmer	2
3. Net Worth	2
4. Residence	2
5. Training and Experience	2
6. Use of Project	2
V INELIGIBLE PROGRAM ACTIVITIES	3
1. Refinance Existing Debt	3
2. Finance Working Capital	3
3. Finance the Acquisition of Property	3
4. Finance a Contract Sale Between a First Time Farmer and Grandparent, Parent or Sibling	3
5. Rural Residence	3
6. CRP Land	3
VI APPLICATION AND PROCEDURES	3
1. Application Forms	3
2. Application Period	3
3. Interim Financing	3
4. Fees	3
5. Use of Financial and Security Documents	3
6. Bond Purchaser	4
7. Public Hearing & Governor's Approval of Bond Issuance	4
8. State Volume Cap Limitations	4
9. Modified Accelerated Cost Recovery System Limitations	4
10. Maximum Loan Maturity	4
11. Purchases from Related Person	4
VII DETAILS FOR DIRECT LOANS	4
1. Loans to First Time Farmers and Security Arrangements	4
2. Terms of Loan	5
3. Repayment of Loan	5
4. Assignment of Sale of Bonds	5
5. Timing Requirements for Spending Bond Proceeds	5
VIII DETAILS FOR SALES CONTRACTS	6
1. Sales Contract and Security Arrangements	6
2. Terms of the Sales Contract	6
3. Payment Under the Sales Contract	7
4. Closing Documents	7
IX LOAN CLOSING PROCEDURES	7
1. Preparation of Legal Notice	7
2. Receipt of Loan Data Sheets and Paperwork Regarding Each Loan	7
3. Preparation of Bond Documents	7
4. Bond Summary	7
5. Request for Governor's Approval	7
6. Prepare for Loan Closing	7
7. Prepare Final Closing Documents	7
8. Verify Returned Closing Documents are Complete	7

X	TAX EXEMPTION OF AUTHORITY BONDS	7
	1. General Federal Tax Exemption of Bonds	7
	2. Federal Alternative Minimum Tax	8
	3. Deduction for Interest Incurred to Carry Tax-Exempt Bonds	8
	4. State Tax Exemption of Bonds	8
XI	MAKING CHANGES AFTER THE BOND IS ISSUED	8
	1. Modifying Interest Rates and Terms	8
	2. Substitution of Collateral & Transfer of Property	8
	3. Disposition of Bonds That Have Been Paid Off	8
XII	RIGHT TO AUDIT	8
XIII	DEFINITIONS	9
	Agricultural Land	9
	Application	9
	Bond Purchaser	9
	Depreciable Agricultural Property.....	9
	Farm.....	9
	First Time Farmer	9
	Indirect Land Ownership	9
	Net Worth.....	9
	Related Person	9
	Substantial Farmland	9

THE PROGRAM SUMMARY IN BREIF

The North Dakota First Time Farmer Finance Program (NDFTFFP) is a tax-exempt bond program designed to assist First Time Farmers in the state of North Dakota to acquire agricultural property at lower interest rates. The Program enables lenders, individuals, partnerships, corporations, and other entities (herein referred to as the "Bond Purchaser") to receive federally tax-exempt interest with respect to a loan or contract sale made to First Time Farmers. The Bond Purchaser, after arranging the loan or sales contract, will obtain from the North Dakota Farm Finance Agency (the "Agency") a federally tax-exempt Private Activity Bond (PAB) in the amount of the loan or unpaid balance. The loan and its collateral will be assigned to the Bond Purchaser as security for the bond. In the case of a contract sale, the contract will be entered into by the Agency, and the Bond Purchaser will receive the bond to evidence the Agency's obligations under the contract. The Agency's right, title and interest in the contract will then be assigned to the First Time Farmer who assumes payment obligations of the Agency under the contract.

Basic Qualifications:

- Net worth of \$500,000 or less (page 9).
- May not have previously owned any substantial farmland (page 9).
- Program may be used to purchase agricultural land, agricultural improvements, and depreciable agricultural property (page 1).
- Property may be purchased from relatives only through third-party lenders (page 4).
- The loan maximums under existing federal laws are:
 - \$469,200 for agricultural land and improvements
 - No more than \$250,000 of the \$469,200 aggregate loan amount can be used for Agricultural Improvements and Depreciable Agricultural Chattel Property. In addition, within the \$250,000 limitation, no more than \$62,500 can be used for Depreciable Agricultural Chattel Property.

There is no minimum loan amount for the program. The Bond Purchaser will make a credit evaluation of the First Time Farmer, may require any collateral deemed necessary and, with the First Time Farmer, must arrange the terms of the loan or contract. The contract or the bond will be limited obligations of the Agency's secured solely by the repayment obligations of the First Time Farmer and collateral provided by the First Time Farmer. The Bond Purchaser will be responsible for the creation and perfection of any security interest deemed necessary for the loan or contract.

A loan made under the Program is funded solely from the bond sold to the Bond Purchaser. The Agency has no independent funds to fund a loan. Therefore, a First Time Farmer must submit an application with Bond Purchaser (bank, contract seller or individual investor) who is able to purchase the Agency's bond to fund the First Time Farmer's loan. The Agency shall not be liable or responsible for the failure of a Bond Purchaser to purchase a bond or otherwise perform the functions of a Lender. Nor shall the Agency be liable or responsible for the failure of a First Time Farmer to locate an alternate Bond Purchaser in the event of a failure of performance by the First Time Farmer's initial Bond Purchaser.

The North Dakota Legislature created the North Dakota Farm Finance Agency in 1997. The Agency's statute is North Dakota Codified Law. The purpose of this law is to assist eligible North Dakotans, who engage in farming or wish to engage in farming, to purchase Agricultural Land, Agricultural Improvements, and Depreciable Agricultural Property. The law also allows for the sale of bonds to individuals for contract sales and direct loans. The Program also allows First Time Farmer loans to be used for transactions between parents, grandparents and siblings. Such transactions can be financed only through third-party lenders; Internal Revenue Service (IRS) rules prohibit contract sales between close relatives.

The powers of the Agency are vested in and exercised by a board of three members. The members consist of the Governor, the Commissioner of Agriculture, and the Attorney General. Bank of North Dakota will administer the program for the Agency.

SECTION I

PROGRAM POWERS AND ELIGIBLE ACTIVITIES

Eligible activities (only for persons who are First Time Farmers) consist of financing of the following:

1. **Agricultural Land (page 9)** -- The Agency can finance the purchase of land suitable for use in farming.
2. **Agricultural Improvements** -- The Agency can finance the construction or purchase of improvements located on Agricultural Land (which are suitable for use in farming). Examples: Confinement systems for swine, cattle, or poultry; barns and other out-buildings; grain storage facilities; silos; improvements to land such as tiling and soil conservation practices which could include, but not be limited to, terraces, farm ponds, erosion control structures, waterways, etc. Agricultural Improvements may be new or used, and may include additions to or renovation of existing buildings or other structures. There are restrictions regarding the financing of a personal residence (page 3) on a farm.
3. **Depreciable Agricultural Property** -- The Agency can finance the purchase of personal property suitable for use in farming for which an income tax deduction for depreciation is allowed in computing Federal income taxes. Example: Livestock used for breeding or dairy purposes, farm machinery, trucks, etc. (feeder cattle, feeder pigs, or feeder lambs do not qualify as Depreciable Property). Bond proceeds may be used to finance new or used Depreciable Agricultural Property). "Used" livestock are female animals that have produced offspring or are male animals that have been used for breeding purposes.

Open or bred heifers, gilts, or lambs would not be considered “used” property under this definition (this class of animals would be considered “new” property). Male animals that have not been used for breeding purposes would also be considered “new” property.

SECTION II

PROGRAM MAXIMUMS AND MINIMUMS

Federal and North Dakota law collectively set various maximum amounts which may be financed under the Program.

1. No more than an aggregate amount of \$450,000 for Agricultural Land, Agricultural Improvements and Depreciable Agricultural Property. It is possible to use the program more than once, if the First Time Farmer still meets eligibility requirements and the total of bonds per individual does not exceed the \$450,000 lifetime maximum.
2. No more than \$250,000 of the \$450,000 aggregate loan amount can be used for Agricultural Improvements and Depreciable Agricultural Chattel Property. In addition, within the \$250,000 limitation, no more than \$62,500 can be used for Depreciable Agricultural Chattel Property.
3. There is no minimum loan amount for the Program.

SECTION III

NATURE OF INVESTMENT RISK: LIMITED OBLIGATION BONDS

THE BOND PURCHASER MUST MAKE THE CREDIT EVALUATION OF THE LOAN OR SALES CONTRACT, THE FIRST TIME FARMER'S NET WORTH, AND ABILITY TO REPAY PRINCIPAL AND INTEREST, AND THE SUFFICIENCY OF THE SECURITY FOR THE LOAN OR SALES CONTRACT. THE AGENCY WILL NOT MAKE AN INDEPENDENT EVALUATION OF THE FIRST TIME FARMER'S ABILITY TO REPAY THE LOAN, PAY THE CONTRACT, OR DETERMINE THE FIRST TIME FARMER'S NET WORTH. THE AGENCY AND ITS COUNSEL WILL NOT REVIEW AND WILL MAKE NO WARRANTIES OR REPRESENTATIONS WITH RESPECT TO THE LEGAL SUFFICIENCY OR VALIDITY OF ANY SALES CONTRACT. In setting the terms and drafting any sales contract, the First Time Farmer and Bond Purchaser are strongly encouraged to consult their legal counsel and tax consultants. The Bond Purchaser will be required to execute a statement at loan closing with respect to his or her understanding of the Agency's limited obligation on the bond and the credit risks inherent in purchasing such a bond. The principal and interest on the bond are limited obligations, payable solely out of the revenue derived from the debt obligation, or sales contract, collateral, or other security furnished by or on behalf of the First Time Farmer. A guarantor, letter of credit or alternative credit enhancement on the debt is permissible. A guarantor may be a Related Person. **The Bond, which is issued by the Agency to the bond purchaser, is a non-recourse obligation of the Agency. The Principal and interest on the Bond do not constitute an indebtedness of the Agency or the state of North Dakota or a charge against their general credit or general funds.** It should also be noted that any recording or filing fees or transfer taxes associated with the loan will be paid by the First Time Farmer or Lender and not the Agency.

SECTION IV

APPLICANT ELIGIBILITY

The basic eligibility requirements for the Program are as follows:

1. **Age Limit** -- First Time Farmer must be at least age 18. There is no upper age limit.
2. **First Time Farmer** -- A First Time Farmer is a person who has never had any direct or indirect ownership interest in Substantial Farmland in the operation of which he/she has materially participated. An ownership interest or material participation by a person's spouse or child will be attributed to the person as well.
3. **Net Worth** -- The First Time Farmer must have a net worth not more than \$500,000.
4. **Residence** -- The First Time Farmer must be a resident of North Dakota at the time the bond is issued.
5. **Use of Project** -- The agricultural land, agricultural improvements and depreciable agricultural property shall only be used for farming by the First Time Farmer, spouse, or minor children.

SECTION V

INELIGIBLE PROGRAM ACTIVITIES

The Internal Revenue Service has promulgated many rules and regulations governing the use and sale of tax-exempt bonds, some of which apply to the Agency's Program. The rules that will affect the Program most are those stating that **tax-exempt bond proceeds cannot be used to:**

1. **Refinance Existing Debt** -that has been incurred by the First Time Farmer more than 60 days prior to the Agency's board approval of a Program application.
2. **Finance Working Capital** -to purchase feed, seed, fertilizer, fuel, etc. (Feeder or pasture cattle, feeder pigs or feeder lambs would also fall into this category).
3. **Rural Residence** - the purchase of only a house is not permitted. However, if the house is a minor part of a farm or acreage purchase it can be included as a part of the loan. No more than 5 percent of the bond proceeds can be used toward the purchase of the house.
4. **CRP Land** - the purchase of farmland that is entirely enrolled in CRP is not permitted. Depending on whether a portion of bond proceeds are financing a house (not to exceed 5 percent) 20-25% of the bond proceeds may be used to purchase CRP acres.

The First Time Farmer, or any "Related Person", shall not make any expenditures with respect to the acquisition or construction of any part of the Project more than 60 days prior to the date the Agency approves the application. To do so runs a risk that the IRS would deem the bond transaction a refinancing; tax-exempt bond proceeds may not be used for the purpose of refinancing.

Notwithstanding the foregoing, approval of an application does not constitute final bond approval. The Agency reserves the right to cease bond processing at any time or to reduce the permitted bond amount, if, prior to bond closing, it is determined that the acquisition is ineligible.

SECTION VI

APPLICATION AND PROCEDURES

A First Time Farmer and Bond Purchaser must prepare and submit an application jointly to the Agency. The following should be noted:

1. **Application Forms** - Application forms are available from the Agency. **The application should be completed by the First Time Farmer and Bond Purchaser and submitted to the Agency.** Applicants and Lenders are encouraged to contact the Agency if they have questions in completing the application.
Current Financial Statement - A copy of the First Time Farmer's current financial statement (taken within 60 days preceding the date of application) must be submitted with the application.
2. **Application Period** - Completed applications (including financial statements) will be acted upon within 5 business days of receipt by the Agency.
3. **Interim Financing (does not apply to contract sales)** - As noted, a First Time Farmer must not make any expenditure with respect to acquisition or construction of any part of the Project more than 60 days prior to the date the Agency approves the application; if this were to occur, the bond transaction could be deemed a refinancing. However, once the application has been approved, the Project may move forward with either construction or possession; if necessary, the Bond Purchaser or another lender may interim finance the loan prior to bond issuance. The interim financing (principal only) will be paid with the proceeds of the bond when issued. The interest on the interim financing is not tax exempt and tax exempt interest will accrue only from the date of issuance of the bond.
4. **Fees** - The First Time Farmer or Bond Purchaser must submit to the Agency a non-refundable \$100 application fee (submitted with the Application). A loan fee equal to 1 percent of the amount of the bond, but not less than \$500, must be paid to the Agency by the First Time Farmer at loan closing. The loan fee may be financed with bond proceeds, or in the case of a contract sale, the loan fee may be included in the purchase price reflected in the sales contract. The Agency's bond counsel will review each bond for legality and tax exemption. The Agency will pay its bond counsel from the fees collected from the First Time Farmer.
5. **Use of Financial and Security Documents** - The Bond Purchaser should use forms of financial statement and security documents which he/she believes are necessary and appropriate under the particular circumstances for the loan or contract sale. These items should be referenced in the bond documents and their provisions incorporated therein. Any additional requirements not specifically provided for in the bond documents, such as insurance coverage and amounts, should also be added.

6. **Bond Purchasers** - It is the Bond Purchaser's responsibility to ensure that any security agreements, mortgages, guarantees or other security documents, which the Bond Purchaser requires in a transaction, have been completed and signed, and that any financing statements have been filed, mortgages recorded or any other necessary steps taken to protect the Bond Purchaser's interests. The Agency makes no warranties or representations with respect to the effectiveness, validity or priority of any liens or security interests which a Bond Purchaser has, or believes he/she may have, with respect to a particular project.
7. **Public Hearing and Governor's Approval of Bond Issuance** - Federal law requires that a public hearing must be held before any Agency bond is issued. A legal notice will be published by the Agency in a regional newspaper of general circulation at least 14 days prior to the hearing. In addition, any individual may file a written request with the Agency at or prior to the scheduled hearing that a local hearing be held in the county where the project is located. Generally, these public hearings will be conducted by the Investment committee of the Bank of North Dakota. However, on some occasions the hearing may be conducted by individual members or by a member of the Agency's staff. A hearing need not be held prior to an Application being approved, but it must be held before the bond documents are approved. The Governor of North Dakota, after receiving a report on the results of the public hearing, may approve or disapprove the Bond.
8. **State Volume Cap Limitations** - The Federal tax law establishes a limit on the total principal amount of tax-exempt Private Activity Bonds which may be issued within any state during a calendar year. In North Dakota, the Volume Cap for each calendar year is \$150 million. All Agency bonds are subject to the limitation. The procedure for the allocation of Private Activity Bonds is set forth by Executive Order 1988-13 dated December 30, 1988. If an allocation from the Volume Cap is not available for a particular bond, the Bond Purchaser and the First Time Farmer will be so advised.
9. **Modified Accelerated Cost Recovery System Limitations** - Bond Purchasers and First Time Farmers should be aware the Federal law limits the application of the Modified Accelerated Cost Recovery System (MACRS) with respect to facilities financed with the Agency's Bonds. If an item is financed with the proceeds of a bond, the First Time Farmer must use an alternative MACRS methods where deductions are computed by applying the straight line method, the applicable averaging convention, and the applicable longer recovery period for such item (12 years for personal property with no class life, 40 years for real property, and the class life for all other property). First Time Farmers should contact their tax consultant regarding how MACRS will affect their operation.
10. **Maximum Loan Maturity** - Federal law provides that the weighted average maturity of an Agency bond can be no more than 120% of the average reasonably expected economic life of the project being financed with the proceeds of the bond (except land).
11. **Purchases From Related Person** - Federal tax law does not allow tax-exempt bonds to be issued to close relatives, including parents, grandparents and siblings ("Related Persons"). Therefore, the purchase of land, improvements or depreciable agricultural property from Related Persons may not be financed by the use of a sales contract; it must be financed by a loan from a third-party lender in order to be eligible. In addition, the Project must be sold to the First Time Farmer for its fair market value. The lender must certify that the Project is being sold for its fair market value and supply an appraisal showing the fair market value of the Project. The Related Person must certify to the Agency that after the sale of the Project to the First Time Farmer the following is/are true:
 - a. If the Project is being operated by a formal or informal partnership or joint venture, the Related Person will have no more than 10 percent interest in such operation;
 - b. If the Project is being operated by a corporation, the Related Person has no more than a 10 percent stock or ownership interest in such corporation;
 - c. If the Project is being operated as a trust, the Related Person has no more than a 10 percent beneficial interest in such trust;
 - d. The Related Person will not be a user of more than 10 percent of the Project; and
 - e. The Related Person will not have any other direct or indirect ownership or use of the Project.

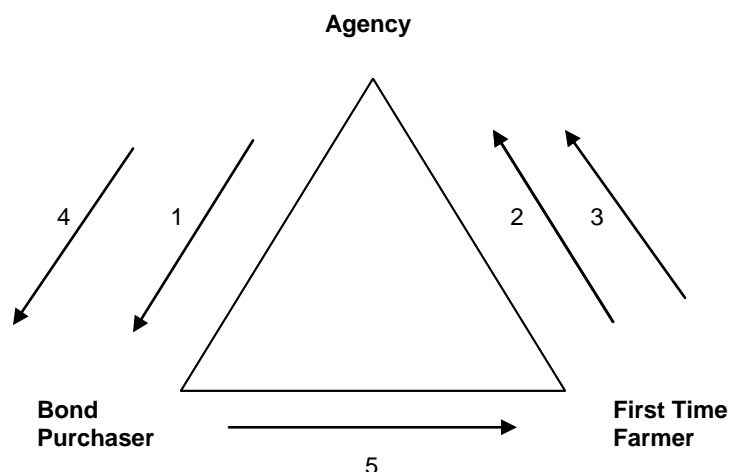
SECTION VII

DETAILS FOR DIRECT LOANS

NOTE: This section applies to transactions involving a direct loan made by the Bond Purchaser to the First Time Farmer. If the First Time Farmer is purchasing the project on a sales contract from the Bond Purchaser, Section VII should be regarded and Section VIII should be followed. IN ALL CASES, ALSO FOLLOW SECTION VI.

1. **Loans to First Time Farmers and Security Arrangements** -- The Program involves the Bond Purchaser, First Time Farmer, and the Authority. The financing is accomplished as follows: in simultaneous transactions the Bond Purchaser purchases the

bond from the Agency; the Agency makes the loan to the First Time Farmer from the proceeds of the bond sale; and then assigns the promissory note it receives from the First Time Farmer to the Bond Purchaser as security for the bond.



- 1) Bond purchased by Bond Purchaser from the Agency;
- 2) Bond proceeds lent by Agency to First Time Farmer;
- 3) First Time Farmer gives promissory note to Agency;
- 4) Promissory note assigned to Bond Purchaser as security for the Bond;
- 5) First Time Farmer makes loan payments to Bond Purchaser.

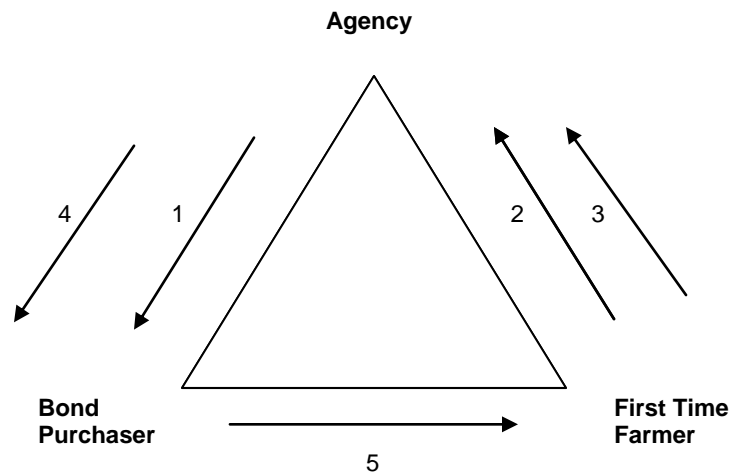
2. **Terms of Loan** - The First Time Farmer and Bond Purchaser must agree on terms of the loan such as interest rate, purchase price, length of loan, prepayment options, service fees, down payment, insurance coverage, security, payment of taxes, repayment schedule, and defaults and remedies on default.
3. **Repayment of Loans** - Under the Agency's bond documents, the First Time Farmer's payment obligations are subject to mandatory prepayment in the event the interest income on the bond becomes includable in gross income for purposes of federal income taxation, in the event that the loan agreement entered into by the First Time Farmer becomes void or enforceable, and to the extent any bond proceeds remain following completion of the acquisition or construction of the Project. In addition, the documents provide for optional prepayment from insurance or condemnation proceeds at the discretion of the Bond Purchaser in the event of damage, destruction or condemnation of any part of the project. The documents also provide for prepayment at the option of the First Time Farmer, the terms and conditions of which are to be agreed upon between the First Time Farmer and the Bond Purchaser.
4. **Assignment or Sale of Bonds** -- The Agency does not place any restrictions on a Bond Purchaser's ability to participate out, assign or sell a bond issued under the Program. Generally, the Bond Purchaser, participating in the Program, purchases the bond for his/her own investment and does not anticipate assigning the bond to another investor. It should be noted there are laws that prevent certain sales and participations, or at least seriously restrict them. For example, the North Dakota Securities Law may impose certain restrictions or requirements if a bond is sold to investors other than financial institutions. In addition, there are adverse federal tax consequences if the bond is assigned, participated out or sold to a "Related Person" of the First Time Farmer. Therefore, a Bond Purchaser should consult with legal counsel to determine if any of these laws or regulations will be violated before selling, assigning, or participating out a bond.
5. **Timing Requirements for Spending Bond Proceeds** -- Federal tax law restrictions generally do not permit the investment of bond proceeds in securities which bear a higher interest rate than the bond. Under the current rules the period of time during which bond proceeds may be invested in an unrestricted yield is eighteen months. The "Gross Proceeds" of a tax-exempt bond must be spent on the project being financed in accordance with the following schedule: (i) 15 percent within 6 months, (ii) 60 percent within 12 months, and (iii) 100 percent within 18 months. If the Bond proceeds are not spent in accordance with such schedule, the parties to the bond issue will be subject to some onerous federal reporting requirements and will be required to pay any profits earned on bond proceeds to the federal government. It should be noted the "Gross Proceeds" of a bond include more than the original principal proceeds. Also included are any amounts earned on the investment of bond proceeds; funds, securities or other obligations (such as a certificate of deposit) which are pledged as security for the payment of the bond. To avoid subjecting any of the Agency's bonds to these reporting and payment requirements, it is the policy of the Agency not to issue a bond for a Project until the Agency can be assured that all bond proceeds will be expended on the Project in accordance with the foregoing schedule. In the closing documents the First Time Farmer and Bond Purchaser are required to certify that the use of the proceeds will comply with this policy.

SECTION VIII

DETAILS FOR SALES CONTRACTS

NOTE: This section applies specifically to transactions involving a sales contract from the contract seller to the First Time Farmer. This section should be disregarded if the Bond Purchaser is making a direct loan to the First Time Farmer and Section VII should be followed. In all cases, also follow Section VI.

1. **Sales Contract and Security Arrangements** -- The Program involves the Bond Purchaser, First Time Farmer, and the Agency. After an application has been submitted and approved, the Bond Purchaser and the Agency will enter into a sales contract and the Bond Purchaser will receive a bond to evidence the Agency's obligations under the contract. The Agency's right, title, and interest in the contract will then be assigned to the First Time Farmer, who will assume the payments and other obligations of the agency under the contract.



- (1) Agency and Bond Purchaser sign sales contract;
(2) Agency assigns the sales contract to the First Time Farmer and delivers a Quit Claim Deed to the First Time Farmer;
(3) First Time Farmer assumes payment obligations under the sales contract;
(4) Agency delivers Bond to Bond Purchaser and assigns the First Time Farmer's obligation to pay sales contract to the Bond Purchaser as security for the Bond;
(5) First Time Farmer makes installment payments on sales contract to Bond Purchaser;
2. **Terms of the Sales Contract** -- It must be clearly stated in the sales contract as to the portion of the payments constituting principal and the portion constituting interest. In addition to other terms the First Time Farmer and Bond Purchaser may include in the sales contract, **the following terms must be included.**
 - (1) This contract will be assigned by the Buyer (North Dakota Farm Finance Agency) to _____ (First Time Farmer) and may not be reassigned by First Time Farmer(s) without the written consent of Seller(s) and the North Dakota Farm Finance Agency which consent, if given, shall not operate as a waiver of the requirement of written consent on any subsequent assignment. Any attempt by First Time Farmer(s) to reassign this contract without written consent shall entitle Seller(s) to declare all amounts due hereunder immediately due and payable.
 - (2) To evidence its payment obligations under this contract, the North Dakota Farm Finance Authority will issue its tax-exempt bond (the "Bond") in an amount equal to the unpaid balance of the purchase price contained herein and bearing interest at the rate of _____ per annum (the "Tax-Exempt Rate") with payment terms identical to those contained herein. First Time Farmer(s) have expressly warranted to Seller(s) that the interest payments received pursuant to the terms contained herein will come to the Seller(s) in the form that will make it not includable in gross income for federal income tax purposes. Seller(s) are relying on the representations made by the First Time Farmer(s) in this regard and in the event the interest payments are determined to be includable in gross income for federal income tax purposes, then all interest payments will be computed on the basis of interest at the rate of _____ per annum (the "Taxable Rate") and First Time Farmer(s) shall be responsible to make payment to the Seller(s) for the difference between interest paid at the Tax-Exempt Rate and the amount calculated on the basis of interest at the Taxable Rate. This provision shall not apply in the event the Bond is held by a Related Person (as defined by the *Internal Revenue Code*) to the First Time Farmer(s). (Note: This paragraph may be modified if a variable rate is used.)

(3) The Seller(s) acknowledges that this contract will be assigned by the North Dakota Farm Finance Agency by separate instrument, the Guarantee, Assignment and Assumption Agreement (the "Guarantee") to the First Time Farmer(s) who will assume the rights, duties, obligations and liabilities of the North Dakota Farm Finance Agency hereunder and guarantee the payment of principal and interest on the Bond. Seller(s) approves such assignment and assumption and acknowledges that the principal of, redemption premium, if any, and interest on the Bond, the installment payments under this contract and other amounts due and owing to the Seller(s) as holder of the Bond and seller under this contract are special limited obligations of the North Dakota Farm Finance Agency and payable solely and only from the obligations of the First Time Farmer(s) under the Guarantee and are not general obligations of the State of North Dakota or any political subdivision or agency thereof, including the North Dakota Farm Finance Agency, within the meaning of any constitutional or statutory limitation and do not constitute or give rise to a pecuniary liability of the State of North Dakota or any political subdivision or agency thereof, including the North Dakota Farm Finance Agency, or a charge against their general credit or general funds.

3. **Payments Under the Sales Contract** - The First Time Farmer's payment obligations and rights and obligations to prepay principal and interest under the sales contract shall be determined by the First Time Farmer and Bond Purchaser and included in the sales contract.
4. **Closing Documents** - The Agency will have no responsibility with respect to the preparation, execution, or filing of any declaration of value statements, groundwater hazard statements, or any other forms or documents as may be required to finalize the transaction.

SECTION IX

LOAN CLOSING PROCEDURES

After the Application receives board approval, the following steps are needed to complete the loan closing process:

1. **Preparation of Legal Notice** - The Agency is required by federal law to publish a legal notice listing each project for which a bond will be issued. This requires consultation with the First Time Farmer of each project to obtain approval for publication of the project listing the amount of the bond, name of applicant, description of project being financed, and exact location of the project, including road identification.
2. **Receive Loan Data Sheets and Paperwork Regarding each Loan** - The Loan/Contract Data Sheet and attachments, as well as appraisals, valuations, and other documents are needed to complete the loan process. The bond purchaser will be required to prepare an amortization or bond payment schedule for the bond and provide the Agency with a copy. First Time Farmers and Bond Purchasers need to allow approximately of two weeks from the time this information is received in the Agency's office to finalize the loan and issue the bond.
3. **Preparation of Bond Documents** - A double set of bond documents will be prepared for each loan. These documents will need signatures by the Bond Purchaser and First Time Farmer at the loan closing.
4. **Bond Summary** - This report is needed for each board meeting so applications/projects can be given final board approval in order that bonds can be issued and loans can be closed. This detailed summary includes all the vital information on each loan, including applicant's name and address, bank name and address, previous approval and publication dates, identification of the project plans, exact location of the project, specific loan terms, and length of loan. This information is obtained from the Loan/Contract Data Sheet submitted.
5. **Request for Governor's Approval** - The Governor needs to approve the issuance of these Private Activity Bonds before they can be issued. These papers then become part of the loan closing documents.
6. **Prepare for Loan Closing** - When final loan documents are returned from the bond attorney's office, the Bond Purchaser or other appropriate individuals are contacted regarding the loan closing date.
7. **Prepare Final Closing Documents** - When the closing date is known, the double set of bond documents and closing papers are dated and finalized. If a contract sale is being done, preparation of a Quit Claim Deed and finalizing of the Sales Contract are also needed. The documents are then sent promptly so the documents are received prior to the closing date.
8. **Verify Returned Closing Documents are Complete** - After loan closing, certain documents need to be returned to the Agency's office. Each packet of materials is reviewed when returned to verify all signatures were obtained and bank seals are affixed where needed.

SECTION X

TAX EXEMPTION OF AUTHORITY BONDS

1. **General Federal Tax Exemption of Bonds** - Under federal tax law an Agency bond is classified as a Qualified Small Issue Bond. Therefore, if all the provisions of the state and federal law continue to be complied with by the First Time Farmer and

Bond Purchaser, the interest on an Agency bond will not be included in the Bond Purchaser's gross income for federal income tax purposes.

2. **Federal Alternative Minimum Tax** - Notwithstanding the preceding paragraph, interest on Agency bonds, which is otherwise tax-exempt, shall be directly includable in the calculation of a bondholder's "alternative minimum taxable income" under section 57(a)(5) of the *Internal Revenue Code* of 1986.
3. **No Deduction for Interest Incurred to Carry Tax-Exempt Bonds** - The Agency bonds are not "qualified tax-exempt obligations" within the meaning of Section 265(c)(3) of the *Internal Revenue Code* of 1986. Accordingly, financial institutions will not be allowed any deduction for that portion of the financial institution's interest expense which is allocable by law to the purchasing or carrying of the Agency's bond. For purposes of the alternative minimum tax, the deduction for *interest expense*, which is allocated to purchasing or carrying tax-exempt obligations and which is otherwise disallowed, shall be used to reduce the amount of tax-exempt interest included pursuant to Section 57(a)(5) in the calculation of alternative minimum taxable income.
4. **State Tax Exemption of Bonds** - Interest on the Agency bond will not be included in gross income of the Bond Purchaser for State of North Dakota income tax purposes (other than the franchise tax measured by net income imposed on banks, trust companies and building and loan associations by North Dakota Century Code Chapters 57-35, 57-35.1, and 57-35.2).

NOTE: The effects of the taxes and deductions discussed above will vary from Bond Purchaser(s) to Bond Purchaser(s) and, as to a given Bond Purchaser, from year to year. Bond Purchaser(s) should consult their regular tax consultants as to the specific effects of these provisions in the Bond Purchaser's tax consequences. The discussion above is for the information and convenience of the Bond Purchaser(s). In no event shall the Agency or its counsel be deemed to have rendered any advice or opinion as to the application of any of the provisions discussed above in a given transaction or to a given Bond Purchaser.

SECTION XI

MAKING CHANGES AFTER THE BOND IS ISSUED

1. **Modifying Interest Rates and Terms** - Interest rates and terms on previously closed loans can be changed or modified. The Agency must approve these changes at a monthly board meeting and issue a resolution reflecting the board action. The following information is needed by the Agency before modifications can be made:
 - a. Project number and borrower(s) name(s).
 - b. Principal balance remaining on the loan.
 - c. New terms - interest rate, payment schedule, etc.
 - d. Effective date of changes.
 - e. The base index rate (not tax-exempt rate) the bank will be using at the time the change will be made.
 - f. The original maturity date of the loan cannot be extended unless a full refunding of the bond takes place. In the case of full refunding, a new bond is written, the old bond is paid off with the proceeds of the new bond, and new terms including maturity date become effective.
 - g. There is a charge for a full refunding but not for a rate change or change of payment dates in which the maturity date is not extended.
2. **Assumption of Loans/Sales Contracts -- Substitution of Collateral & Transfer of Property** -- Loans or sales contracts may not be assumed without the prior approval of the Agency, and then only if the new purchaser of the property will qualify as a First Time Farmer. Equipment and other depreciable property may be exchanged or traded for similar property, and other property such as breeding livestock may be added or substituted as collateral at the discretion of the Bond Purchaser without the prior approval of the Agency. The benefits of the Agency bond must remain with a qualified First Time Farmer, and no person to whom property is traded or otherwise transferred may obtain the benefits of the bond.
3. **Disposition of Bonds That Have Been Paid Off** -- When a bond matures and the loan is paid off, the following information is needed:
 - a. The original bond issued by the Agency to fund the loan (on green check paper) needs to be returned to the Agency marked "paid" and the date it was paid off. A copy of the bond marked "paid" should be given to the First Time Farmer.
 - b. If it is a bank loan, a copy of the Promissory Note marked "paid" and date paid should be sent to the Agency with the original given to the First Time Farmer.
 - c. The Bond Purchasers should make copies of these documents for file if they wish to retain them for a record.
 - d. Other than the bond, the Agency does not want the bond documents returned that were issued for the loan. The Bond Purchaser should retain these for record purposes.

SECTION XII

RIGHT TO AUDIT

The Agency shall, at any time, have the right to audit or monitor records of the Bond Purchaser and the First Time Farmer relating to a loan and bond to insure the bond proceeds were used for qualified purposes by a qualified user.

SECTION XIII

DEFINITIONS

The definitions used in the Program are important to Bond Purchasers and First Time Farmers contemplating using the Program.

Note: The ability to finance a personal residence with the Program is severely limited due to federal regulations governing the use of the Agency's bonds; therefore, except in certain circumstances (e.g., when the value of the residence is clearly less than 5% of the amount of the loan or the amount of contract financed), it will be necessary to finance the personal residence separately.

"Agricultural Land" - Land suitable for use in farming and which is or will be operated as a farm.

"Application" - A completed instrument on a form approved by the Agency. Each application must include the following: First Time Farmer's name, address, financial data, description of anticipated use of loan proceeds, amount of loan or contract sale to be financed, down payment amount (if any), statement of First Time Farmer's net worth determined in accordance with Agency rules, a summary of proposed loan or contract terms and certifications of the First Time Farmer and Bond Purchaser. Each Application must be accompanied by the First Time Farmer's financial statement (taken within 60 days of Application submission).

"Bond Purchaser" - Any individual, lender, corporation, business trust, estate, trust, partnership or association, or any other legal entity that obtains an Agency bond under the Program in connection with a contract sale or loan to a First Time Farmer.

"Depreciable Agricultural Property" - means personal property suitable for use in farming for which an income tax deduction for depreciation is allowable in computing federal income tax under the Internal Revenue Code of 1986.

"Farm" - means a farming enterprise which is recognized in the community as a farm rather than a rural residence.

"First-Time Farmer" - An individual who has a net worth of not more the \$500,000 and has never had any direct or indirect ownership interest in "Substantial Farmland" in the operation of which he or she has materially participated. An ownership interest or material participation by an individual's spouse or minor child will be attributed to the person as well. However, the Federal tax law also provides that an individual's prior ownership interest in farmland will be disregarded if:

- a. Such Farmland was disposed of while the person was insolvent; and,
- b. Section 108 of the Internal Revenue Code applied to the indebtedness with respect to such farmland; that is the individual was not required to recognize any income for federal tax purposes from the cancellation of the indebtedness of the farmland loans.

"Indirect Land Ownership" - If a person holds a minimal interest in a family farm corporation, a limited partnership, a trust, or any other type of entity which in turn owns farmland in an amount which is greater than 30 percent of the median size of a farm in the county, and the person materially participates in the operation of such farmland, then the person will not qualify as a First Time Farmer.

"Net Worth" - Total assets minus total liabilities as determined in accordance with generally accepted accounting principals with appropriate exceptions and exemptions reasonably related to an equitable determination of the First Time Farmer's net worth. Assets shall be valued at fair market value.

"Related Persons" - according to the IRS, includes grandfather, grandmother, father, mother, brother or sister (whether whole or half blood), child, grandchild or spouse. It also includes certain corporations and partnerships. (see page 3)

"Substantial Farmland" - Any parcel of land is "Substantial Farmland" unless the parcel is smaller than 30 percent of the median size of a farm in the county where the parcel is located.